

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B04

PLR-137164-08

Date:

July 10, 2009

In Re:

Legend:

Decedent =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Spouse =

Attorney =

Law Firm =

a =

b =

c =

d =

e =

f =

Trust =

Trustee =

Dear :

This responds to a letter dated July 31, 2008, and subsequent correspondence submitted by your authorized representative, requesting an extension of time under § 301.9100-3 of the Procedure and Administration Regulations to sever a trust into a qualified terminable interest (QTIP) trust and non-QTIP trust under § 20.2056(b)-7(b)(2)(ii) of the Estate Tax Regulations, and for additional rulings with respect to the severed trusts.

Facts

Decedent, a resident of State, died on Date 1 survived by Spouse and three children. Under Article VII of his will, Decedent bequeathed \$a to Spouse outright and the remainder of his residuary estate to a trust ("Trust"). Under the terms of Trust, the Trustee is to pay or apply to or for the use of Spouse during her lifetime, at least quarter-annually, the net income of Trust. In addition, the Trustee may at any time or from time to time pay to Spouse so much of the principal, whether the whole or a lesser amount, as the Trustee, in his sole discretion, may determine. Upon the death of Spouse, \$b of Trust principal is to be distributed to Decedent's daughter, and the remainder is to be distributed to Decedent's issue (including daughter) in equal shares, per stirpes. Decedent's will authorized the executor of his estate to make the qualified terminable interest property (QTIP) election for all or any portion of Trust. However, the will did not specifically authorize the Trustee to divide the Trust into a QTIP trust and a non-QTIP trust in the event that a partial QTIP election was made, nor did it expressly authorize the severance of either trust into a generation-skipping transfer (GST) exempt trust and a GST non-exempt trust.

As executrix of Decedent's estate, Spouse retained the services of Attorney at Law Firm to prepare Decedent's Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return. Decedent's estate tax return was timely filed on Date 2. On Schedule M, a QTIP election was made for an undivided portion of Trust consisting of c% of Trust's value in the amount of \$d. The Form 706 did not evidence any intent to divide the Trust into two separate trusts, a QTIP trust and a non-QTIP trust. On Schedule R, Decedent's entire GST exemption amount of \$e was allocated to the undivided Trust. Decedent's GST exemption amount was less than the value of the undivided Trust and less than the value of the portion of the Trust for which the QTIP election was made. As a result of the allocation, Trust has an inclusion ratio of .5197. Also, pursuant to the instructions on Schedule R, the allocation is deemed to be an election under § 2652(a)(3) to treat the undivided portion of Trust for which the QTIP election was made on Schedule M as if the QTIP election had not been made for GST tax purposes (reverse QTIP election).

The executrix received a letter dated Date 3 from the Internal Revenue Service indicating that the Decedent's Form 706 had been accepted as filed and that no estate tax was due. The administration of Decedent's estate was closed and a Final Accounting was rendered on Date 4.

Affidavits submitted in connection with this ruling request affirm the representation that the Attorney at Law Firm who prepared Decedent's Form 706 did advise Spouse, as executrix, to make the QTIP election for that portion of Trust that was in excess of Decedent's unused exemption equivalent amount. However, the Attorney neither advised Spouse to sever the Trust into a QTIP trust and a non-QTIP trust and to indicate such intent on the Form 706, nor did she advise Spouse to divide the QTIP trust into a GST exempt trust and a GST non-exempt trust. Attorney did advise Spouse to allocate Decedent's GST exemption amount to the Trust on Schedule R, resulting in a reverse QTIP election for the QTIP portion of the undivided Trust.

Trustee of Trust requests the following rulings:

1. That an extension of time be granted under § 301.9100-3 of the Procedure and Administration Regulations and § 20.2056(b)-7(b)(2)(ii) of the Estate Tax Regulations to sever the Trust into two trusts, a QTIP trust constituting c% of the Trust assets (as elected on Schedule M of Form 706) and a non-QTIP trust constituting f% (the balance) of the Trust assets; that the severance will be effective as of the date of Decedent's death for estate tax purposes; and that following the severance, under local law, the terms of Decedent's will will govern each separate trust.
2. That the QTIP trust will be a "reverse QTIP" trust under § 2652(a)(3) and, based on the allocation made on Schedule R of Form 706, the QTIP trust and the non-QTIP trust will each have an inclusion ratio of .5197.
3. That the QTIP trust may be severed in a qualified severance under § 26.2642-6(d)(7)(ii) of the Generation-Skipping Transfer Tax Regulations into two trusts, one with 48.03 percent of the QTIP trust assets, and one with 51.97 percent of the QTIP trust assets; that after the qualified severance, the trust with 48.03 percent of the QTIP trust assets will be a "reverse QTIP" trust with an inclusion ratio of zero, and the trust with 51.97 percent of the QTIP trust assets will be a "reverse QTIP" trust with an inclusion ratio of one; that the qualified severance will be effective prospectively from the date of such severance and, after such date, in accordance with local law, the terms of Decedent's will will govern each of the separate trusts.
4. That the non-QTIP trust may be severed in a qualified severance under § 26.2642-6(d)(7)(ii) of the regulations into two trusts, one with 48.03 percent of the non-QTIP trust assets and one with 51.97 percent of the non-QTIP trust assets; that after the qualified severance, the trust with 48.03 percent of the non-QTIP trust assets will have an inclusion ratio of zero, and the trust with 51.97 percent of the non-QTIP trust assets will have an inclusion ratio of one; that the qualified severance will be effective prospectively from the date of such severance and, after such date, in accordance with local law, the terms of Decedent's will will govern each of the separate trusts.

Law and analysisRuling Request 1

Section 2001(a) imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2056(a) provides that for purposes of the tax imposed by § 2001, the value of the taxable estate is to be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse.

Under § 2056(b)(7), a marital deduction is allowed for qualified terminable interest property (QTIP), which is defined under § 2056(b)(7)(B) as property (i) which passes from the decedent, (ii) in which the surviving spouse has a qualifying income interest for life, and (iii) to which the election under § 2056(b)(7)(B)(v) applies. Section 2056(b)(7)(B)(v) provides that the election with respect to any property shall be made by the executor on the return of tax imposed by § 2001 and, once made, shall be irrevocable.

Section 20.2056(b)-7(b)(2)(i) of the Estate Tax Regulations provides that the QTIP election may relate to all or any part of property that meets the requirements of § 2056(b)(7)(B)(i), provided that any partial election must be made with respect to a fractional or percentage share of the property. The fraction or percentage may be defined by a formula.

Section 20.2056(b)-7(b)(2)(ii)(A) provides that, in general, a trust may be divided into separate trusts to reflect a partial election that has been made, or is to be made, if authorized under the governing instrument or otherwise permissible under local law. Any such division must be accomplished no later than the end of the period of estate administration. If, at the time of the filing of the estate tax return, the trust has not yet been divided, the intent to divide the trust must be unequivocally signified on the estate tax return.

In the present case, Decedent's will did not specifically authorize the Trustee to divide the Trust into two separate trusts to reflect the partial QTIP election. Nonetheless, section 7-1.13(a) of State's Estates, Powers and Trusts law (EPTL) authorizes an executor or trustee, without court approval or the consent of the beneficiaries, to establish two or more separate trusts in order to segregate property held in trust in which a spouse has a qualifying income interest for life and for which a QTIP election was made from property with respect to which no QTIP election was made. Under section 7-1.13(b), such a division relates back to the effective date of the disposing instrument. Further, under section 7-1.13(c), the terms of the disposing instrument shall govern each separate trust. Section 7-1.13(f) defines "disposing instrument" as a will,

trust agreement, instrument exercising a power of appointment or other instrument creating such a trust or transferring property to such trust. If separate trusts are established under § 7-1.13(a), § 7-1.13(e) requires that they be established by an instrument or instruments in writing, signed and acknowledged by the trustee and filed in the office of the clerk of the court having jurisdiction over the trust. Under § 7-1.13(d), where the original assets remain or can be traced, the property distributed to the separate trust shall be fairly representative of appreciation or depreciation and shall be based upon the fair market value of the assets on the date or dates of the distributions of such assets to the separate trusts.

Under § 301.9100-1(c), the Commissioner may grant a reasonable extension of time under the rules set forth in §§ 301.9100-2 and 301.9100-3 to make a regulatory election, or a statutory election (but no more than 6 months except in the case of a taxpayer who is abroad), under all subtitles of the Code except subtitles e, G, H, and I.

Sections 301.9100-1 through 301.9100-3 provide the standards the Commissioner will use to determine whether to grant an extension of time to make a regulatory election.

Section 301.9100-2 provides for automatic extensions for time for making certain elections.

Section 301.9100-3(a) provides that, in general, requests for extensions of time for regulatory elections that do not meet the requirements of § 301.9100-2 must be made under the rules of § 301.9100-3. Requests for relief subject to § 301.9100-3 will be granted when the taxpayer provides the evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the Government.

Section 301.9100-3(b)(1)(iii) provides that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer failed to make the election because, after exercising reasonable diligence (taking into account the taxpayer's experience and the complexity of the return or issue), the taxpayer was unaware of the necessity for the election.

Section 301.9100-3(b)(1)(v) provides that a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer reasonably relied on a qualified tax professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

Based on the facts presented and the representations made, we conclude that the requirements of § 301.9100-3 have been satisfied. Accordingly, Trustee is granted sixty (60) days from the date of this letter to sever the Trust into two trusts, a QTIP trust constituting c% of the Trust's assets (as elected on Schedule M of Form 706) and a non-QTIP trust constituting f% (the remainder) of the Trust's assets. The severance will

be effective as of the date of Decedent's death for estate tax purposes and, under § 7-1.13(c) of State's EPTL, the terms of Decedent's will will govern each separate trust. Trustee should file a supplemental Form 706 within 60 days from the date of this letter unequivocally signifying the severance of the Trust. The supplemental Form 706 should be filed with the Internal Revenue Service Center, Cincinnati, Ohio 45999. A copy of this letter should be attached to the return.

Ruling Request 2

Section 2601 imposes a tax on every generation-skipping transfer (GST). Section 2611 defines a GST as (1) a taxable distribution, (2) a taxable termination, and (3) a direct skip.

Section 2602 provides that the amount of tax is the taxable amount multiplied by the applicable rate. Section 2641(a) defines "applicable rate" as the product of the maximum federal estate tax rate and the inclusion ratio with respect to the transfer.

Section 2642(a) provides that the inclusion ratio is determined by subtracting the applicable fraction from 1. Section 26.2642-1(b) and (c) of the Generation-Skipping Transfer Tax Regulations provides, in relevant part, that the numerator of the applicable fraction is the amount of GST exemption allocated to the trust, and the denominator of the applicable fraction is the value of the property transferred to the trust.

As in effect for the year of Decedent's death, § 2631(a) provides that, for purposes of determining the inclusion ratio, every individual shall be allowed a GST exemption of \$1,000,000 (adjusted for inflation under § 2631(c)) which may be allocated by such individual (or by his executor) to any property with respect to which such individual is the transferor. Section 2631(b) provides that once an allocation of GST exemption is made, it is irrevocable.

Section 2632(a) provides that any allocation by an individual of his GST exemption may be made at any time on or before the date prescribed for filing the estate tax return for such individual's estate (including extensions).

Section 2652(a)(3) provides that in the case of any trust with respect to which a deduction is allowed to the decedent's estate under § 2056(b)(7), the estate of the decedent may elect to treat all of the property in the trust, for purposes of the GST tax, as if the election to be treated as QTIP had not been made. The election is referred to as the reverse QTIP election. The consequences of a reverse QTIP election is that the decedent remains, for GST tax purposes, the transferor of the QTIP trust for which the election is made. As a result, the decedent's GST exemption may be allocated to the QTIP trust.

Section 26.2652-2(b) provides that the reverse QTIP election is to be made on the return on which the QTIP election is made.

As noted above, Decedent's entire GST exemption of \$e was allocated to Trust on Schedule R of Form 706. Pursuant to the instructions on Schedule R, the allocation of Decedent's GST exemption to Trust is deemed to be an election under § 2652 (a)(3) to treat the portion of the Trust for which the QTIP election was made on Schedule M as if the QTIP election had not been made for GST tax purposes. As a result of the allocation of Decedent's GST exemption to Trust, Trust has an inclusion ratio of .5197.

Accordingly, we conclude that after Trust is severed into a QTIP trust and a non-QTIP trust, the QTIP trust will continue to be treated as a reverse QTIP trust and each of the new trusts will continue to have an inclusion ratio of .5197.

Ruling Requests 3 and 4

Section 2642(a)(3)(a) provides that if a trust is severed in a qualified severance, the trusts resulting from such severance shall be treated as separate trusts thereafter for GST purposes. A qualified severance is defined under § 2642(a)(3)(B) as the division of a single trust and the creation (by any means available under the governing instrument or under local law) of two or more trusts if the single trust was divided on a fractional basis, and the terms of the new trusts, in the aggregate, provide for the same succession of interests of beneficiaries as are provided in the original trust. If a trust has an inclusion ratio of greater than zero and less than 1, a severance is a qualified severance only if the single trust is divided into two trusts, one of which receives a fractional share of the total value of all trust assets equal to the applicable fraction of the single trust immediately before the severance. In such case, the trust receiving such fractional share shall have an inclusion ratio of zero and the other trust shall have an inclusion ratio of 1. Section 2642(a)(3)(C) provides that a qualified severance may be made at any time.

Section 26.2642-6(d)(7)(i) provides that in the case of a qualified severance occurring after GST tax exemption has been allocated to a trust, if the trust has an inclusion ratio that is greater than zero and less than one, then the requirements of either § 26.2642-6(d)(7)(ii) or (iii) must be satisfied.

Section 26.2642-6(d)(7)(ii) provides that where a trust is severed initially into only two resulting trusts, one resulting trust must receive that fractional share of the total value of the original trust as of the date of severance that is equal to the applicable fraction used to determine the inclusion ratio of the original trust immediately before the severance. The other resulting trust must receive that fractional share of the total value of the original trust as of the date of severance that is equal to the excess of one over the fractional share described in the preceding sentence. The trust receiving the fractional

share equal to the applicable fraction shall have an inclusion ratio of zero, and the other trust shall have an inclusion ratio of one.

In the present case, Decedent's will did not specifically authorize the Trustee to divide the Trust into separate trusts for GST purposes. However, section 7-1.13(a) of State's EPTL authorizes an executor or trustee, without court approval or the consent of the beneficiaries, to establish two or more separate trusts in order to segregate property held in trust which is exempted from the GST tax from property that is not so exempt, so that one of the trusts will have an inclusion ratio of zero and the other will have an inclusion ratio of one. Under section 7-1.13(b) of State's EPTL, such a division relates back to the effective date of the disposing instrument. Unlike the severance of the Trust into a QTIP trust and a non-QTIP trust under Ruling 1, however, the effective date of a qualified severance is the date of the severance, and the resulting trusts are treated as separate trusts for GST purposes as of that date. Under State's EPTL, § 7-1.13(c), the terms of Decedent's will will govern each separate trust.

Therefore, based on the facts submitted and representations made, we conclude that the reverse QTIP trust and the non-QTIP trust (which will be a separate trusts under Ruling 1) may each be severed in a qualified severance under § 2642(a)(3) and § 26.2642-6(d)(7)(ii) into two trusts, provided that the severances are reported to the Service following the requirements of § 26.2642-6(e). One of the reverse QTIP trusts will contain 48.03 percent of the reverse QTIP trust assets and will have an inclusion ratio of zero, and the other will contain 51.97 percent of the reverse QTIP trust assets and have an inclusion ratio of one. Similarly, one of the non-QTIP trusts will contain 48.03 percent of the non-QTIP trust assets and will have an inclusion ratio of zero, and the other will contain 51.97 percent of the non-QTIP trust assets and will have an inclusion ratio of one.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any transaction or item discussed or referenced in this letter.

This letter is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely.

Curtis G. Wilson
Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures: copy for section 6110 purposes
copy of letter

cc: